Remarks by
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Secretary of Navy
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Mr. McGrath, thank you for that kind introduction. It is great to be back for my third appearance before this group.

In 2006, I spoke to you about the lack of long-term alignment between industry and the Navy.

Not to be outdone in terms of candor, last year my message of "tough love" to the Navy and the shipbuilding industry was about our need to make significant changes together.

This year, after having worked on those issues inside the Department for more than two years, I would like to give you my assessment of the changing landscape shaping the Navy-industrial partnership.

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I approach the issue of acquisition with a long-term perspective.

The Navy as a service is forced to adopt a long-term horizon due to the lead times necessary to build capital ships that can take up to a decade to design and build, and which are expected to remain in service for 40 years or more.

Thus, we would do well to keep in mind that old dictum—given today's relatively supportive budget environment—that people are tempted during favorable times to avoid thinking that there might come a change, for it is human nature when the sea is calm not to think of storms.

Mariners cannot afford to make this mistake.

We must look at our shipbuilding program now, and position the fleet for a time when, as many have said, "there might come a change."

Everyone in this room should understand that we may soon face a growing budgetary challenge.

We cannot count on continued growth in the top line of our budget—and yet we are experiencing increasing cost pressures from many quarters.

We have to be prepared to operate in a less favorable budget environment.

The Department of Defense budget has gone from around $300 billion seven years ago, to over $500 billion today.

Some of that additional spending has gone into acquisition.

But we cannot expect to sustain the increases in acquisition account investment that we have seen in recent years.

Congress has, of late, been very supportive of shipbuilding investments.

But it is neither prudent nor wise to count on future administrations and future Congresses to continue support at ever-increasing levels.

Given the evolving budgetary environment, the challenge for us is to ensure that the Navy can continue to build the force we need in an affordable manner.

It is particularly important that the Navy—an organization that is necessarily capital-intensive—demonstrate cost effectiveness with taxpayer dollars.

We must position ourselves such that future Congresses and future administrations will support our plans to build a 313-ship Navy, deliver the next generation of Naval aircraft, and fund the full complement of Marine Corps expeditionary assault capabilities that the Navy and Marine Corps depend on for the execution of our core missions.

Our current recapitalization and modernization path will require significant improvements in efficiency if we are to reach 313 ships in a timely manner.

Business as usual will not get us there.

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We know that we must come up with a cost-effective way of building the fleet.

On the Navy's end, we are making significant changes to improve our performance in acquisition.

To achieve that, we have implemented an acquisition governance program that forces more senior leadership engagement, enhanced transparency, and greater discipline at every phase of the acquisition lifecycle.

Unprecedented collaboration, coordination, and systems engineering have been codified in a two pass, six gate review process which synchronizes both requirements and acquisition issues throughout the entire life cycle of a program—with senior leadership engagement at the highest levels, throughout.

This governance process is a good step towards achieving acquisition improvement.

The overriding objective is to implement changes that will facilitate our ability to make better decisions early in the acquisition process.

That combined with detailed design criteria, more comprehensive specifications, and better use of cost data will result in greater stability in our requirements.

Greater requirements stability is also a function of appetite suppression—we cannot have what we want, only what is needed, as the CNO aptly summed up in his remarks two days ago.

All of these changes will provide us with a basis for realizing better cost control, more timely delivery, improved system availability and improved operational utility.

We recognize that we still have a long way to go to put acquisitions on a better path.

That is why the Department is also focusing on workforce re-engineering in the areas of systems engineering, program management, and contract management.

I will also note that I am most pleased to see the extent to which CNO and the Commandant of the Marine Corps are supporting this effort, which leaves me optimistic that these changes will endure well into the future.

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Now, making better decisions on our end, and improving the entirety of the acquisitions process, will help, but it is not enough.

Changes on the part of the Navy must be matched by a commitment from industry to make the investments necessary to materially improve the efficiency of its development and production processes.

Our objective is the timely delivery of mission-capable and available assets that are produced at an affordable and predictable price.

This will necessitate significant industry investments in people, processes, and facilities—not unlike what the world's leading shipbuilders have done over the past ten years.

The Navy understands that for corporations to make these investments, we must motivate them to do their part to rebuild a viable industrial base.

I have traveled to many foreign shipyards during my tenure as Secretary, and I have learned that shipyards tackle the need for efficiency in many different ways.

One example is found in Denmark, whose shipbuilders have figured out a way to compete internationally—despite high labor costs.

Their shipbuilders use simple, but capable, structures; they design for small crews; and they build ships using highly automated processes.

Notably, they have demonstrated an ability to apply common design principles and manufacturing techniques for the construction of both commercial and military ships.

This formula has allowed them to compete successfully with Chinese and South Korean shipyards that have far lower labor costs.

Now, some have suggested that highly automated production lines are only economical for low density ships produced in high volumes.

But there are, in fact, shipyards with high levels of automation that exclusively build surface combatants.

The VT shipyard in Portsmouth, England that builds the Type 45 destroyer provides us with a compelling example.

Portsmouth shipbuilders have shown that even in a shipyard dedicated solely to military construction, they can leverage available technology in a modern controlled environment to build surface combatants based on multiple levels of modularity, with extensive outfitting.

Our yards can learn from the Danes, the British, and others that the technology is commercially available and applicable to warship production.

The US shipbuilding industry needs to adopt the best practices of the world's shipbuilders.

I am happy to note that some of this technology is already being adopted on the later DDG 51s and is poised for utilization in DDG 1000 production.

In a day and age when most U.S. shipbuilders are owned by defense conglomerates, it is all the more important that corporate leaders understand that shipbuilding is fundamentally different from most of the defense industry in that the world-class standard is typically found overseas.

Through a careful analysis of technologies and best practices already in existence abroad, our private shipyards can identify a vision for the industrial base of the future, and their position in it.

We understand that from an industry perspective, necessary investments will only take place if a reasonable rate of return can be expected—and if those returns are competitive with alternative investment options.

Investment decisions in most defense companies are typically justified by new business opportunities enabled by those investments.

But the shipbuilding business model is quite different from that followed by much of the defense and aerospace industry.

Given a variety of factors, including physical plant limitations and workforce constraints, competition for shipbuilding contracts is very limited.

When a competition does occur, it is typically a competition on the margin, and not a full and open competition for business in the traditional sense.

For example, the follow-on DDG 1000 competition for the remaining five ships of the class will be a competition for quantity—not a winner-take-all.

Nonetheless, there is and will continue to be a competition for taxpayer investments in national security, for our ability to manage the costs of shipbuilding will determine how many ships we can build, and what our fleet will look like.

This competition for national security investments will determine how much work is contracted with our private shipyards, and how much profit will be potentially available.

Inherent in this calculus is a rationale for investment that needs to be recognized by our contractors and reinforced by the Navy.

Both the Navy and our shipbuilders have a common vested interest realizing improved shipyard efficiencies.

I am concerned that the Nation may well decide to invest elsewhere if our shipbuilding industry does not more aggressively modernize.

I do not want to see the U.S. Navy follow the lead of other nations, whose leadership has basically decided that they cannot afford a modern Navy.

The way forward is going to require a collaborative effort between industry and the Navy to develop an investment strategy that industry will be motivated to support, and that can provide the affordable fleet that our Navy so urgently needs.

Given that our FAR processes provide mechanisms that enable contractors to recapture the costs of personnel development, process improvements, and facility modernization, it is not unreasonable for the Navy to expect those contractors to make material investments in shipbuilding.

I am very supportive of finding ways to further incentivize industry to increase investments, but I do not accept the grant concept as an appropriate way to achieve this objective.

Furthermore, I would encourage industry to identify any additional investment recommendations that offer the potential of a win-win for Navy and industry.

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As I have said in the past, industry will have to take the lead on its plans for improving and investing in facility and process efficiency.

Industry taking the lead in its own investment does not preclude the Navy from being a partner.

Recent examples of incentive-based investment resulting from the Navy-industry partnership have included the VIRGINIA class capital expenditure—or CAPEX—program.

Another excellent example is the proposal that General Dynamics made to the Navy for investment in its Ultra Hall facility at Bath Iron Works to achieve efficiencies on DDG production.

In lieu of providing additional funding, the Navy offered an early release of withholds from current contracts to facilitate the investment.

This case was an example of a win-win for both General Dynamics and the Navy.

And after the destruction of Hurricane Katrina, Northrop Grumman Shipbuilding Gulf Coast approached First Marine International to obtain help in identifying best practices, and implement alternative processes that will help shape the rebuilt shipyard.

As another example, NASSCO is collaborating with a subsidiary of Daewoo Shipbuilding and Marine Engineering to build nine product carrier tankers for the Jones Act trade.

NASSCO builds auxiliary ships for the Navy, and we are encouraged by the prospect of construction learning opportunities across platforms.

We've seen investments in people as well.

A notable example of the kind of investment in people that I have in mind is taking place at the Northrop Grumman Shipbuilding Newport News operation, which has invested heavily in its apprenticeship school.

Its training program has set an industry standard.

We would hope to see more of these types of innovative proposals from all of our suppliers.

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I will conclude by saying something that I have said before.

There is no silver bullet, no single point solution, and no single accounting change that will solve the efficiency and modernization challenges in the shipbuilding industry.

We have instituted governance changes which will more closely marry our requirements and acquisition processes, resulting in more stability in requirements in our long-term plan.

But we understand that the way forward will require dramatic improvements in our collective processes across the board.

Together, we can make this happen.

Together, we can achieve the 313 shipbuilding plan with an affordable budget and reasonable returns on investment.

And, most importantly, together, we can continue to keep our Navy the number one sea power in the world.

Thank you all for your many contributions to our Nation's security, and may God continue to bless America.